

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF BIG RIVERS)	
ELECTRIC CORPORATION FOR APPROVAL)	
OF THE 1998 AMENDMENTS TO STATION)	
TWO CONTRACTS BETWEEN BIG RIVERS)	CASE NO. 98-267
ELECTRIC CORPORATION AND THE CITY)	
OF HENDERSON, KENTUCKY AND THE)	
UTILITY COMMISSION OF THE CITY OF)	
HENDERSON)	

O R D E R

By Order dated April 30, 1998 in Case No. 97-204,¹ the Commission approved new rates for Big Rivers Electric Corporation ("Big Rivers"), and approved in principle a 25 year lease of its generating units to a subsidiary of LG&E Energy Corp. The Commission's decision was based on the transaction as reflected in the documents filed as of February 27, 1998. However, since many of the documents were revised after that date, the Commission directed that the final drafts of all jurisdictional documents be submitted in this case for a determination of whether material changes have been made to the structure of the transaction.

This case was established on May 15, 1998 when Big Rivers filed the 1998 Amendments to Station Two Contracts which relate to its operation of the City of Henderson's Station Two Generating Plant. Over the next 45 days, Big Rivers filed the

¹ The Application of Big Rivers Electric Corporation, Louisville Gas and Electric Company, Western Kentucky Energy Corp., Western Kentucky Leasing Corp., and LG&E Station Two Inc. For Approval of Wholesale Rate Adjustment for Big Rivers Electric Corporation and For Approval of Transaction.

final drafts of all transaction documents. A procedural schedule was entered providing all parties an opportunity to engage in discovery and a public hearing was held on July 6, 1998.

The Commission notes at the outset that this is anything but a routine review of documents relating to a rate adjustment and asset lease. Big Rivers is a debtor in possession under Chapter 11 of the United States Bankruptcy Code. The documents under review are essential and critical components of Big Rivers' plan of reorganization as approved by the Bankruptcy Court on June 1, 1998. All of the parties to Case No. 97-204 were made parties to this case. Most of them participated to some extent in this case, but no party objected to any of the documents under review herein. The absence of any objection, however, does not diminish the Commission's obligation to ensure that there have been no material changes in the transaction. This obligation takes on greater importance here since the term of the lease is 25 years and the power contracts have terms that extend up to 25 years.

Based on a comprehensive analysis of the final drafts of the transaction documents, the Commission finds that there have been several material changes made to the structure of the lease transaction. The most current economic analysis of the lease transaction, filed by Big Rivers on July 7, 1998 and identified as PSC2-38R, has been compared to the one identified as SUP-11, which formed the basis for our conditional approval in Case No. 97-204. To the extent the transaction has undergone a material change, it is discussed herein.

Transmission Service for Smelter Loads

The documents on file with the Commission as of February 27, 1998 provided as follows with respect to the Smelters' transmission service:

- 1) Green River Electric Corporation ("Green River") and Henderson Union Electric Cooperative Corp. ("Henderson Union") would arrange for and reserve transmission on Big Rivers' transmission system for Tier 1 Energy, Tier 2 Energy, and Tier 3 Energy purchased from LG&E Energy Marketing Inc. ("LEM") for resale to Southwire Company ("Southwire") and Alcan Aluminum Corporation ("Alcan").²
- 2) Transmission services were to be provided at Big Rivers' Open Access Transmission Tariff ("OATT") rates.³
- 3) Green River and Henderson Union were responsible for all transmission costs and were entitled to a transmission credit against the total payments owed to LEM. The credit equaled the amount the cooperative paid to Big Rivers for the transmission of Tier 1 Energy, Tier 2 Energy, Tier 3 Interruptible Energy, and Tier 3 Backup Energy.⁴
- 4) LEM would pay to the RUS, on behalf of Big Rivers, a monthly smelter margin payment ("monthly margin payments"), which reflected the net

² See Case No. 97-204, Document filing of February 23, 1998, Volume III, Tabs 15 and 16, at 8-12. The reference is to the Amendments to the Wholesale Power Agreements between Big Rivers and Green River and Big Rivers and Henderson Union, Paragraphs 3 and 4.

³ Id. at 11.

⁴ See Case No. 97-204, Documents filed February 27, 1998, the Agreements between Henderson Union and LEM and Green River and LEM, Schedule A, part g.

smelter margins originally included in Big Rivers' financial model. The monthly margin payments would remain fixed regardless of the amount of power actually supplied by LEM to the Smelters and the payments specifically excluded any transmission service revenues.⁵

Big Rivers, the LG&E Parties, and the Smelters had strongly stressed the significance of the guaranteed monthly margin payments and the significant benefit this arrangement represented to Big Rivers.⁶ The Commission accepted this argument, noting in the April 30, 1998 Order that the guarantee of the smelter margins was an improvement to the overall transaction, which the Commission approved in principle.

The changes made to the transaction documents reviewed in Case No. 97-204 include the following relating to transmission service for the Smelters' load:

- 1) LEM will arrange for and reserve transmission on Big Rivers' transmission system for Tier 1 Energy, Tier 2 Energy, and Tier 3 Energy. LEM will continue to provide Green River and Henderson Union with the energy resold to the Smelters, with the types and amounts of transmission reserved by LEM for these sales being referred to as Member Transmission.⁷

⁵ See Case No. 97-204, Supplemental Testimony of A. J. Robison, Stephen Schaefer, and Mark A. Hite, at 4, 5, and 8.

⁶ See Case No. 97-204, Transcript of Evidence, Volume VI, March 18, 1998, at 11-12, 15, and 48; Big Rivers Supplemental Initial Brief at 14-16; LG&E Parties Initial Brief Addressing Future Unforeseen Cost Issue at 3; Alcan and Southwire Supplemental Brief on Unforeseen Cost Resolution at 4-5.

⁷ Document filing of May 29, 1998, Volume II, Tab 8, at 19-25. The reference is to the Transmission Service and Interconnection Agreement, Sections 6.5.1. and 6.5.2.

- 2) LEM will continue to pay the monthly margin payments to the RUS on behalf of Big Rivers. However, these payments have been revised to include the revenue for smelter transmission service, which was originally shown separately in the Big Rivers financial model.⁸
- 3) As long as the full monthly margin payments are made pursuant to the terms of the transaction agreements, Big Rivers will deem the full cost of the Member Transmission to have been paid at the then applicable OATT rate as part of the monthly margin payments. Consequently, LEM's cumulative cost for Member Transmission charged by Big Rivers will never exceed the cumulative amount of the monthly margin payments.⁹

The impact of these changes on Big Rivers is that if its OATT transmission rate increases, it will no longer recover the full smelter margin payments and its cost of transmission service. The margin payments are now to be reduced by any increase in transmission rates above the levels agreed to by the Smelters.

Big Rivers contends that it had always borne the economic risk of future changes in transmission costs as applied to the fixed wholesale power rates for service to the Smelters for which the monthly margin payments are to be received. Big Rivers argues that the designation of a portion of the monthly margin payments as a transmission payment at OATT rates in no way changes the economic positions of Big Rivers and the

⁸ Response to the Commission's June 12, 1998 Order, Item 7, page 37 of 81.

⁹ Document filing of May 29, 1998, Volume II, Tab 8, at 22-23.

LG&E Parties, but merely provides Big Rivers with the same economic risk regarding transmission which it has always had.¹⁰

The significant changes to the smelter transmission arrangements presented by Big Rivers and the LG&E Parties have affected the Commission's evaluation of the overall lease transaction. The documents upon which the Commission based its April 30, 1998 approval in principle stated that smelter transmission service would be obtained at OATT rates. At that time, the monthly margin payments excluded transmission service revenues, making it impossible to adjust the payments for transmission cost changes. The revisions proposed in this proceeding allow the smelter margins modeled by Big Rivers to be used to offset any shortfall in transmission revenues resulting from the actual OATT rates exceeding the transmission rates agreed to by the Smelters. In the event of such a shortfall in transmission revenue, the proposed revisions to the smelter transmission service will result in lower overall revenues to Big Rivers and expose its non-smelter customers to potential rate increases.

Big Rivers contends that it has always borne this economic risk, and that the proposed revisions do not change the arrangement that was part of the unforeseen cost resolution. The documents on file with the Commission as of February 27, 1998 do not support this position. Based on those documents, Green River and Henderson Union had the initial risk of fluctuations in OATT rates for the smelter load transmission service; however, the transmission credit appeared to shift this risk to LEM. The revisions proposed in this proceeding now shift that risk back to Big Rivers.

¹⁰ Response to the Commission's June 12, 1998 Order, Item 13(c), page 7 of 10.

Big Rivers has contended that it does not expect its transmission rates, as modeled in its financial model,¹¹ to change during the terms of the Smelters' contracts. Big Rivers claims that it is just as likely that its transmission rates will decrease as increase, but has offered no analysis or study to support its claim.

The Commission finds it likely, however, that for Big Rivers to improve its ability to make arbitrage sales, it may have to join an Independent System Operator ("ISO") to eliminate transmission rate pancaking. In the event the transmission rates established for the ISO are higher than Big Rivers' OATT, under the proposed revision, Big Rivers is faced with a no win situation. If it does not join an ISO, its ability to make critical arbitrage sales could be restricted. If it does join, it would incur additional costs for transmitting power to the Smelters, but would be unable to recover those costs from LEM or the Smelters. Big Rivers' inability to recover these costs would put pressure on its overall financial condition, and could eventually result in higher rates for its remaining customers.

Having considered all of the factors discussed herein, the Commission will accept the designation of LEM, rather than Green River and Henderson Union, as the party responsible for arranging and reserving transmission service with Big Rivers. The Commission also accepts the inclusion of the transmission revenues from the Smelters, as shown in Big Rivers' financial model, in the monthly margin payments. However, the

¹¹ The latest update of Big Rivers' financial model, identified as PSC2-38R, shows transmission rates through 2006 at \$.98/KW/month. In 2007, the rate for network transmission appears to increase to \$1.02/KW/month while non-firm point-to-point transmission is priced at \$1.04/KW/month. In the year immediately after the Smelter contracts are scheduled to expire, all transmission is shown at the \$1.04/KW/month rate.

Commission finds unreasonable the provision that allows increases in the OATT rates charged to LEM, except as modeled originally by Big Rivers, to be offset by the remaining portion of the monthly margin payment. That portion of the monthly margin payment reflecting the modeled net smelter margins exclusive of transmission revenues should remain as described in the documents on file with the Commission as of February 27, 1998.

In determining an equitable methodology for the recovery of unforeseen increases in transmission costs due to the Smelters' load, the Commission will be guided by the unforeseen cost resolution previously negotiated by the parties to the transaction. Under this approach, for any increase in Big Rivers' OATT rate in excess of that included in its financial model, 50 percent of the excess will be charged to LEM as part of its transmission costs. The bundled rates charged by LEM to Green River and Henderson Union will be equally adjusted. Consequently, the bundled rates charged by Green River and Henderson Union to Southwire and Alcan, respectively, will be adjusted to reflect the 50 percent of the increase in transmission costs. In the event that Big Rivers' OATT rate falls below the transmission rate included in its financial model, the rates charged to LEM, Green River, Henderson Union, Southwire, and Alcan will not be reduced. Any revenues in excess of the OATT rates should be retained by Big Rivers as an offset to the \$1.85 million payment it makes each year as its 50 percent contribution to resolve the Smelters' indemnification for future unforeseen costs.

Agreement for Electric Service to Commonwealth Industries, Inc.

One of the documents filed in this proceeding was a draft of a new Agreement for Retail Electric Service ("Agreement") between Green River and Commonwealth

Industries, Inc. ("Commonwealth"). As a preliminary matter, the Commission notes that filing of this Agreement was not anticipated. There was no indication by any party in Case No. 97-204 that the agreement for service to Commonwealth would be subject to any additional negotiations or revisions. Apparently, one or both of the parties to the Agreement were dissatisfied with the Commission's April 30, 1998 Order in Case No. 97-204, and seized the opportunity presented by this instant case to submit a revised contract for electric service. Although the Agreement is not within the intended scope of this case, in the interest of administrative efficiency we will consider the merits of the Agreement.

This Agreement, when compared to one reviewed in Case No. 97-204, contains several changes which tend to favor the interests of Commonwealth over those of Green River and its wholesale power supplier, Big Rivers. The most significant of these changes is the establishment of two primary levels of power and billing for service to Commonwealth: (1) Peaking Power - defined as power and associated energy taken at 35,000 KW and above at a load factor of 10 percent or less, up to a maximum of 5,000 KW; and (2) all other power ("non-peaking power") and associated energy, taken at 35,000 KW and below.

Under its previous agreement, Commonwealth was required to take-or-pay for the full \$10.15 demand charge applied to its contract demand of 40,000 KW, regardless of its actual demand level. Under the proposed Agreement, Commonwealth's non-peaking demand will be capped at a maximum of 35,000 KW to which the \$10.15 demand charge will be applied. All energy taken up to the 35,000 KW level will be billed at Big Rivers' wholesale energy rate plus a retail energy adder of \$.0003 per KWH. For

the Peaking Power, all demand in excess of 35,000 KW would incur no demand charge, but would be billed a "peaking energy charge of \$0.075" per KWH plus the retail adder previously mentioned.

Commonwealth contends that, compared to its previous agreement, this Peaking Power provision provides it with the proper financial incentive to manage its operation processes to eliminate the short term surges in power consumption that occur on its system from time to time. These surges in consumption cause its billing demand to spike above its 35,000 KW contract demand.¹² Commonwealth also argues that the pricing terms included in the proposed Agreement will produce a revenue level closer to the level envisioned in the Commission's April 30, 1998 Order in Case No. 97-204. Commonwealth makes these assertions based on its historic demand and energy billing units for calendar years 1996-1997.

Based on a review of the merits of the proposed Agreement, the Commission finds that it should be rejected. None of the proponents of the Agreement have shown good cause to justify granting Commonwealth terms or prices for electric service that are more favorable than those available to others within the same customer class, i.e. non-smelter industrial customers served from dedicated delivery points. A demand charge of \$10.15 for each KW in excess 35,000 KW will provide Commonwealth with a far greater financial incentive to avoid surges in consumption than will the proposed Peaking Power energy rate.

¹² In Case No. 97-204, Big Rivers modeled a continuous demand level of 35,000 KW for Commonwealth throughout the 25-year planning horizon without recognizing any "needle peaks" or "spike demands" in excess of 35,000 KW.

Particularly unpersuasive are Commonwealth's arguments regarding its annual electric bill as calculated under: 1) the rates proposed by Big Rivers in Case No. 97-204; 2) the rates approved by the Commission in Case No. 97-204; and 3) the rates under this proposed Agreement. Commonwealth's Exhibit 2, which is intended to be an analysis of its annual electric bill and the corresponding level of revenues flowing to Big Rivers, is misleading. The Commission did not design rates for only the 1996 normalized test year, as implied in this exhibit. The billing units in Commonwealth's Exhibit 2 do not correspond to those included in the Big Rivers' financial model which the Commission utilized to develop rates for Commonwealth and all other members of its class for the entire 25-year term of the lease transaction.

Commonwealth has calculated its annual electric bill to be higher than what it might have expected because it utilized a demand level consistently higher than the 35,000 KW included in Big Rivers' model. Had Commonwealth utilized its expected demand level of 35,000 KW, its calculation of revenues would have been less by \$487,200 per year.¹³

Customers' electric bills and the corresponding level of utility revenues are affected by both the rates and the customers' usage. It would be pure coincidence if Commonwealth or any other customer consumed power at levels identical to those in the normalized historic test year or the 25-year forecast. Commonwealth cannot reasonably expect to receive special treatment merely because it now asserts that its consumption levels will differ from those incorporated into the Big Rivers' model.

¹³ (468,000 KW * \$10.15) = \$4,750,200
less: (420,000 KW * \$10.15) = \$4,263,000 equals \$487,200.

Capital Budgets

On April 6, 1998, Big Rivers and the LG&E Parties executed a document entitled "New Participation Agreement," which replaced the original Participation Agreement and the Amended and Restated Participation Agreement contemplated by the lease transaction. This New Participation Agreement reflected changes in the transaction documents related to the resolution of the unforeseen cost issue, as well as clarifications of the parties' intent and the correction of errors.¹⁴ On June 10, 1998, Big Rivers and the LG&E Parties filed a document entitled "Second Amendment to the New Participation Agreement" ("Second Amendment"). The Second Amendment reflected numerous clarifications and corrections to the majority of the lease transaction documents, reflected the decisions announced in the Commission's April 30, 1998 Order, and resolved uncertainties related to environmental issues. In addition, the Second Amendment addressed and resolved differences of opinion between Big Rivers and the LG&E Parties concerning the appropriate composition of the annual capital budget.¹⁵

Subsequent to filing the documents in February 1998 to resolve the unforeseen cost issue, Big Rivers and the LG&E Parties discovered there were significant differences between the amounts each party projected for the annual capital budgets for Big Rivers' generating plants. At that time, there was no upper limit on Big Rivers' exposure for non-incremental capital costs, which were reflected in the annual capital budget. Thus, the annual capital budget levels represented a major area of uncertainty

¹⁴ Response to the Commission's June 12, 1998 Order, Item 7, page 5 of 81.

¹⁵ Id., pages 13 through 22 of 81.

in Big Rivers' financial modeling. As reflected in the Second Amendment, the LG&E Parties agreed to limit Big Rivers' exposure to unlimited increases in the annual capital budgets. Big Rivers had originally projected non-incremental capital costs to be \$83.8 million over the life of the lease transaction. The Second Amendment capped this total exposure at \$147.7 million, an increase of \$63.9 million over the transaction term.¹⁶

While the Commission can appreciate Big Rivers' desire to limit its exposure to increases in the capital budgets, the impacts of incurring an additional \$63.9 million in costs on Big Rivers' financial model should be considered. Big Rivers was requested to provide an update of the SUP-11 version of its financial model that reflected the lease transaction as described in the documents filed in this case. The ending cash balance at the end of the lease term was shown in SUP-11 as \$171.8 million.¹⁷ The updated financial model, PSC2-38R,¹⁸ showed that the ending cash balance at the end of the lease term was \$24.8 million.¹⁹ The difference between the SUP-11 and PSC2-38R versions of the financial model reflected numerous revisions to the financial model,

¹⁶ Response to the Attorney General's First Information Request, Item 4, pages 2 and 3 of 5.

¹⁷ See Case No. 97-204, Supplemental Testimony of A. J. Robison, Stephen Schaefer, and Mark A. Hite, Supplemental Exhibit 11, Printout of File SUP11.WK4, Year 2022, Line 404.

¹⁸ Big Rivers had originally filed an updated financial model, PSC2-38, in its response to the Commission's June 23, 1998 Order, Item 38. However, at the public hearing on July 6, 1998, Big Rivers indicated that it had discovered some errors in that filing and submitted the revised financial model, PSC2-38R, as Big Rivers Cross-Examination Exhibit No. 2.

¹⁹ Big Rivers Cross-Examination Exhibit No. 2, File PSC2-38R.WK4, Year 2022, Line 326.

including the additional \$63.9 million in non-incremental capital costs provided by the terms of the Second Amendment.

The Commission finds that the modifications to the annual capital budgets required by the Second Amendment are reasonable and should be approved. However, this and other modifications contained in Big Rivers' financial model heighten concerns about Big Rivers' financial condition during the later years of the lease. In the April 30, 1998 Order, the Commission required Big Rivers to file a supplemental annual report comparing its actual cash flows for the calendar year with the amounts included in the SUP-11 financial model. The report was to be based on lines 363 through 411 of SUP-11, and include explanations for any deviations from the SUP-11 amounts in excess of 10 percent. The Commission will continue this requirement, but will substitute the updated financial model PSC2-38R for SUP-11, with the report now based on lines 285 through 333 of PSC2-38R. In addition, to better monitor Big Rivers' financial condition over the term of the lease transaction, Big Rivers will be required to submit with its annual report an updated version of its financial model.²⁰ The updated financial model will cover the period beginning with the current annual report year and ending with the last year of the lease transaction. All changes in assumptions and variables from one year to the next should be explained in detail.

Revolving Credit Agreement

On June 26, 1998, Big Rivers filed a copy of a revolving credit agreement ("Credit Agreement") it has entered into with the National Rural Utilities Cooperative

²⁰ One hard copy of the updated financial model and one computer disc version should be provided.

Finance Corporation ("CFC"). Under the terms of the Credit Agreement, CFC will provide Big Rivers a maximum aggregate principle amount outstanding of \$15 million. For each 12-month period the Credit Agreement is in effect, Big Rivers will be required to reduce to zero all amounts outstanding for at least five consecutive business days, with the first reduction due within 360 days of the first advance. The term of the Credit Agreement is 5 years. Big Rivers believes that the CFC Credit Agreement does not require Commission approval.

The Commission's jurisdiction to approve evidences of indebtedness is set forth in KRS 278.300. Specifically excluded from that jurisdiction under KRS 278.300(8) is the approval of notes payable at periods of not more than 2 years from the date issued and renewable for not more than a total of 6 years. The Commission finds that the terms of the CFC Credit Agreement fall within this exemption and, therefore, we agree with Big Rivers that no Commission approval is needed.

Smelters' Tier 3 Service Contracts

The proposed power contracts between Green River, Henderson Union, and the Smelters contain specific provisions concerning contracts for Tier 3 service from third-party power suppliers. When seeking Commission approval to make a sale of Tier 3 power to the Smelters, Green River and Henderson Union are contractually obligated to request that such approval be effective 20 days from the date of notice.²¹ However, KRS 278.180(1) requires a minimum of 30 days notice prior to changing a rate, unless good cause is shown to shorten the notice period to 20 days. Green River and

²¹ See Agreement for Electric Service between Alcan and Henderson Union and Agreement for Electric Service between Southwire and Green River, Section 9.2.

Henderson Union have indicated that the parties would accept a revision to the power agreements that reflects the 30-day statutory requirement.²²

The Commission finds that the power agreements between Green River, Henderson Union, and the Smelters should be revised to reflect the 30-day notice provision set forth in KRS 278.180(1). Including this notice in the power agreements will not prevent any of the parties to those agreements from requesting a shorter notice period on a case-by-case basis when a Tier 3 service contract is filed.

Promissory Note for LEM Advances

Big Rivers has requested that the Commission approve the promissory note associated with the LEM advances, noting that such approval was omitted from the April 30, 1998 Order in Case No. 97-204. While we believe that note to have been implicitly approved by that Order, the Commission now explicitly finds that the promissory note for the LEM advances is for a lawful object within Big Rivers' corporate purpose, is necessary and appropriate for the proper performance of its wholesale electric service to the public and will not impair its ability to perform that service, and is reasonably necessary and appropriate for such purpose.

1998 Amendments to the Station Two Contracts

Big Rivers has requested that the Commission approve the 1998 Amendments to the Station Two Contracts, which were filed with the Commission on May 15, 1998. The Commission finds that these documents are reasonable and should be approved.

²² Response to the Commission's June 23, 1998 Order, Item 20.

Green River Wholesale Contract Amendment, Schedule 1

On June 6, 1998, Big Rivers submitted a substitute Schedule 1 to its wholesale power agreement with Green River. The substitute Schedule 1 reflects the inclusion of the proposed new service agreement between Green River and Commonwealth. Based on the decision herein to reject the new Commonwealth agreement, the Commission rejects the substitute Schedule 1 to the wholesale power agreement.

Standby Bond Purchase Agreements

On June 24, 1998, Big Rivers filed Standby Bond Purchase Agreements ("Standby Agreements") related to its 1983 and 1985 Pollution Control Bonds ("1983 and 1985 Bonds") and Credit Suisse First Boston, the new provider of letters of credit for those bonds. The Standby Agreements were required as part of the rating agencies' evaluation of the 1983 and 1985 Bonds. Big Rivers requested that the Commission permit the late filing of the Standby Agreements in this case.

As the Standby Agreements are an integral part of the overall financial restructuring of Big Rivers' obligations, the Commission will permit the late filing and hereby approves the Standby Agreements as part of all other financial agreements presented in this proceeding.

Confidentiality Petition for Marketing Plan

As part of its April 30, 1998 Order in Case No. 97-204, the Commission required Big Rivers to file an interim sales plan which would address how Big Rivers planned to pursue arbitrage sales opportunities until the lease transaction closed. On May 29, 1998, Big Rivers filed its Interim Sales Plan and a petition for confidential treatment of that document. On June 18, 1998, Alcan and Southwire responded to the petition,

requesting a modification to the petition that would permit all parties to Case No. 97-204 who have executed appropriate confidentiality agreements to obtain copies of the Interim Sales Plan. On June 23, 1998, Big Rivers filed its reply to the Smelters' response, expressing its opposition to the request. At the July 6, 1998 public hearing, Big Rivers requested that the Commission include a ruling on the petition for confidential treatment in its Order in this proceeding.

The Commission finds that it is not appropriate to rule on Big Rivers' petition for confidentiality or the Smelters' request for access in this proceeding. The Interim Sales Plan was filed in Case No. 97-204, and the petition and request will be adjudicated in that case. In addition, the Commission finds no reason to modify its normal procedures for the processing of requests for confidentiality.

Distribution Cooperative Tariff

Green River and Henderson Union have submitted proposed Smelter tariffs to the Commission for approval. The proposed tariffs incorporate both the agreements for electric service between the cooperatives and the respective Smelters and Schedule A of those agreements, which details the terms and rates for Smelter service. Alcan and Southwire have notified the Commission of their opposition to incorporating the agreements for electric service into the tariffs, contending that the proposed tariffs only need to incorporate Schedule A. At the July 6, 1998 hearing the Smelters identified this disagreement as an issue for the Commission to address in this Order.

The Commission finds that there has been no evidence offered by the Smelters to justify the exclusion of the agreements for electric service from the smelter tariffs as filed with the Commission. Consequently, the Commission will not require Green River

or Henderson Union to remove the language incorporating the agreements for electric service from the proposed tariffs.

Jurisdiction over OATT

On July 1, 1998, Big Rivers, Alcan, Green River, Henderson Union, and Southwire filed a joint motion requesting that the Commission assert jurisdiction over Big Rivers' OATT to the extent that the Federal Energy Regulatory Commission ("FERC") does not assert jurisdiction over the OATT. The July 1, 1998 motion notes that Big Rivers' status as a generation and transmission cooperative, combined with the limited jurisdiction of FERC over such entities, creates a "regulatory gap" in jurisdiction over many provisions of the OATT. The parties to the July 1, 1998 motion request that the Commission fill this regulatory gap by asserting jurisdiction, subject to five specific limitations enumerated in the motion.

Big Rivers was formed pursuant to the requirements of KRS Chapter 279. KRS 279.210 provides that every corporation formed under that chapter shall be subject to the general supervision of the Commission and shall be subject to all the provisions of KRS 278.010 to 278.450 inclusive, and KRS 278.990. Therefore, to the extent that FERC has not asserted jurisdiction over Big Rivers' OATT, the Commission will do so, in accordance with KRS Chapters 278 and 279. However, the Commission will assert this jurisdiction without the specific limitations referenced in the July 1, 1998 motion, as the applicants have not demonstrated why the expression of such limitations are necessary or reasonable.

Fuel Adjustment Clause Cases

Big Rivers has requested that, concurrent with our decision in this case, all pending fuel adjustment clause ("FAC") cases be dismissed. Motions to dismiss are currently pending in each of those FAC cases. While the FAC cases have not been consolidated with the instant case, the Commission recognizes their importance to the closing of Big Rivers' lease transaction. Therefore, Orders will be issued in the near future holding in abeyance those FAC cases that have been remanded to the Commission and that are not directly affected by the Franklin Circuit Court Order of June 29, 1998 in Civil Action No. 94-CI-01184. Those cases will be closed once Franklin Circuit Court recalls and vacates its Judgment of October 20, 1995 in that action. As to those cases that are directly affected by the Franklin Circuit Court Order of June 29, 1998, we find that the motions to dismiss are moot and Orders to that effect will be issued by the Commission in the near future. As to all remaining FAC cases, the Commission intends to issue Orders in the near future closing those cases without the need for further action by Big Rivers.

SUMMARY AND CONCLUSION

As announced in the April 30, 1998 Order in Case No. 97-204, the purpose of this proceeding was to review the final drafts of all jurisdictional documents to determine whether any material changes had been made to the lease transaction. As discussed in this Order, material changes have been made in the areas of smelter transmission service and Big Rivers' funding obligations to the annual capital budgets.

While we have denied the proposed methodology for the recovery of unforeseen increases in transmission costs due to the Smelters' load, we believe that the approved

methodology represents a fair and reasonable solution. While we have accepted the modifications to the annual capital budgets, these changes will be costly to Big Rivers over the next 25 years. Consequently, Big Rivers' long-term financial survival is not a certainty but, rather, is a goal that will have to be achieved by management. Critical to meeting this goal will be the successful marketing of power off-system. A greater degree of Commission monitoring will also be necessary and, thus, we have established additional financial reporting requirements for Big Rivers. The Commission remains optimistic that with continued hard work and dedication by Big Rivers, its financial viability will be assured and it will prosper hand-in-hand with the economy of Western Kentucky.

IT IS THEREFORE ORDERED that:

1. Based on the final drafts of all documents filed in this proceeding, Big Rivers' proposed lease transaction with the LG&E Parties is approved, subject to the modifications contained in this Order.
2. The proposed methodology for the recovery of unforeseen changes in transmission costs due to the Smelters' load is denied.
3. A 50/50 sharing methodology for the recovery of unforeseen changes in transmission costs due to the Smelters' load, as discussed in this Order, is approved.
4. The proposed revision to Schedule 1 of the Green River Wholesale Power Contract with Big Rivers and the proposed new agreement between Green River and Commonwealth are denied.
5. Ordering Paragraph No. 21 of the April 30, 1998 Order in Case No. 97-204 is modified to the extent that the PSC2-38R financial model, lines 285 through 333,

shall replace the reference to the SUP-11 financial model, lines 363 through 411. In addition, Big Rivers shall annually file an updated version of its financial model with its annual report to the Commission, covering the period beginning with the current annual report year and ending with the last year of the lease transaction. All changes in assumptions and variable from one year to the next shall be explained in detail.

6. All evidences of indebtedness required to be issued by Big Rivers in conjunction with the transaction documents are approved, including the LEM Promissory Note and the Standby Agreements. The CFC Credit Agreement is exempt from Commission approval.

7. The Smelter Tier 3 Service Contracts are modified to provide the Commission with 30 days notice of effectiveness, in accordance with KRS 278.180(1).

8. The 1998 Amendments to the Station Two Contracts are approved.

9. The Smelters' objection to the form of the Green River and Henderson Union Smelter Tariffs is overruled.

10. Big Rivers' OATT filed in this proceeding is hereby approved and the OATT shall be subject to the jurisdiction of this Commission to the extent that FERC has not asserted jurisdiction and preempted this Commission.

11. Within 30 days of the date of this Order, Big Rivers shall file its tariffs, reflecting all revisions and modifications as described in this Order.

12. Ordering Paragraph Nos. 13, 15, 16, 18, 20, and 22 of the April 30, 1998 Order in Case No. 97-204 shall remain in full force and effect as if separately ordered herein.

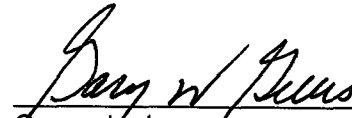
Nothing contained herein shall be construed as a finding of value for any purpose or as a warranty on the part of the Commonwealth of Kentucky, or any agency thereof, as to the securities authorized herein.

Done at Frankfort, Kentucky, this 14th day of July, 1998.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:


Executive Director